

ST 98-11

Tax Type: SALES TAX

Issue: Responsible Corp. Officer - Failure to File or Pay Tax

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
SPRINGFIELD, ILLINOIS**

THE DEPARTMENT OF REVENUE)	
OF THE STATE OF ILLINOIS)	
)	Docket No.
v.)	Reg. #
)	NPL #
JOHN & JOE DOE)	
Respondents, as responsible officers)	
of ABC, Inc.)	

RECOMMENDATION FOR DISPOSITION

Appearances: Charles Hickman, Special Assistant Attorney General, for the Department of Revenue of the State of Illinois; Richard C. Kirby of Erwin, Martinkus & Cole, Ltd. for JOHN & JOE DOE.

Synopsis:

The Department of Revenue ("Department") issued Notices of Penalty Liability ("NPLs") to JOHN and JOE DOE ("respondents") pursuant to section 13½ of the Retailers' Occupation Tax Act ("ROTA")¹ as it is incorporated into the Motor Fuel Tax Law (Ill.Rev.Stat., ch. 120, par. 434a, now 35 ILCS 505/12). The NPLs allege that the respondents were officers or employees of ABC, Inc. ("corporation") who were responsible for wilfully failing to pay the corporation's motor fuel taxes ("MFT"). The respondents timely protested the NPLs. An evidentiary hearing was held during which

¹ At the time that the tax liability became due, the relevant provision was Ill.Rev.Stat. 1991, ch. 120, par. 452½. This section has been replaced by section 3-7 of the Uniform Penalty and Interest Act (35 ILCS 735/3-7).

the respondents presented documentary evidence and testimony from JOHN DOE. After reviewing the record, it is recommended that this matter be resolved in favor of the Department.

Findings of Fact:

1. The respondents were the sole officers and directors of the corporation. (Tr. pp. 6-7)

2. The respondents admitted that they were responsible for filing MFT returns and paying the taxes to the Department on behalf of the corporation. (Resp. brief, p. 3)

3. The respondents were aware that the corporation was having financial difficulties. (Tr. pp. 12, 23)

4. On October 1, 1991, the corporation entered into an agreement to sell its assets to FICTITIOUS FUEL COMPANY. (Resp. Group Ex. #1; Tr. pp. 7-8)

5. The attorney for FICTITIOUS FUEL COMPANY notified the Department that it was going to purchase the corporation's assets. On October 16, 1991, the Department issued a Bulk Sales Stop Order to FICTITIOUS FUEL COMPANY. (Resp. Group Ex. #1)

6. JOHN DOE testified that the Department agreed to release the Stop Order if the Department received \$60,000 from the proceeds for the sale of the assets. (Tr. p. 25)

7. At the closing for the sale of the assets, the respondents received \$100,000, of which \$60,000 was paid to the Department and \$40,000 to Citizens Bank of CITY ("Citizens Bank"). Citizens Bank was a secured creditor and would not release its security interest in the corporation's assets without the \$40,000 payment. The \$60,000 was paid to the Department on November 21, 1991. (Resp. Ex. #2; Tr. pp. 9-10)

8. JOHN DOE testified that he believed that the \$60,000 payment to the Department covered the total liability owed to the Department by the corporation. (Tr. pp. 25-26)

9. On October 3, 1991, the corporation owed \$55,265.05 to creditors other than the Department and Citizens Bank. (Resp. Ex. #3; Tr. pp. 11-13)

10. XYZ COMPANY was the corporation's major supplier. From June to October of 1991, XYZ COMPANY would not deliver supplies to the corporation without receiving payment in advance by wire transfers. (Resp. Group Ex. #4-8; Tr. pp. 15-16)

11. JOHN DOE admitted that he did not prepare a MFT return for July 1991. Sometime in February of 1992 the Department prepared the July 1991 return for the corporation. Steven agreed with the Department's figures on the return. (Resp. Ex. #9; Tr. pp. 26-27, 31-33)

12. The corporation's only checking account from June through October of 1991 was at Citizens Bank. (Resp. Group Ex. #4-8; Tr. pp. 14-15)

13. The respondents had signature authority on the corporation's checking account. (Tr. pp. 22, 24)

14. From June through October of 1991, the corporation made several payments to unsecured creditors. During the months of August, September, and October, the corporation paid over \$9,000 to various unsecured creditors, such as JOHN & JOE DOE, utility companies, an accounting firm, and a law firm. (Resp. Group Ex. #4-8; Resp. brief pp. 3-4)

15. On March 3, 1993, the Department issued NPL number 5192 to JOHN DOE and NPL number 5203 to JOE DOE. Each NPL proposed a penalty liability for failure to pay MFT for the months of June through October of 1991. The NPLs were admitted into evidence under the certificate of the Director of the Department. (Dept. Ex. #1).

Conclusions of Law:

Section 13½ of the Retailers' Occupation Tax Act provides in part as follows:

"Any officer or employee of any corporation subject to the provisions of this Act who has the control, supervision or responsibility of filing returns and making payment of the amount of tax herein imposed in accordance with Section 3 of this Act and who wilfully fails to file such return or to

make such payment to the Department or willfully attempts in any other manner to evade or defeat the tax shall be personally liable for a penalty equal to the total amount of tax unpaid by the corporation, including interest and penalties thereon;" Ill.Rev.Stat. 1991, ch. 120, par. 452½ (now 35 ILCS 735/3-7(a)).

An officer or employee of a corporation may therefore be personally liable for the corporation's taxes if (1) the individual had the control, supervision or responsibility of filing the MFT returns and paying the taxes, and (2) the individual willfully failed to perform these duties.

Under section 13½, the Department's certified record relating to the penalty liability constitutes *prima facie* proof of the correctness of the penalty due.² See Branson v. Department of Revenue, 168 Ill.2d 247, 260 (1995). Once the Department presents its *prima facie* case, the burden shifts to the respondent to establish that one or more of the elements of the penalty are lacking, i.e., that the person charged was not the responsible corporate officer or employee, or that the person's actions were not willful. Id. at 261. In order to overcome the Department's *prima facie* case, the allegedly responsible person must present more than his or her testimony denying the accuracy of the Department's assessment. A. R. Barnes & Co. v. Department of Revenue, 173 Ill.App.3d 826, 833-34 (1st Dist. 1988). The person must present evidence that is consistent, probable, and identified with the respondent's books and records to support the claim. Id.

In this case, the Department's *prima facie* case was established when the Department's certified record relating to the penalty liability was admitted into evidence. In response, the respondents do not argue that they were not responsible for filing the MFT returns. They contend, however, that they did not willfully fail to pay the taxes.

² The relevant portion of section 13½ provides as follows: "The Department shall determine a penalty due under this Section according to its best judgment and information, and such determination shall be *prima facie* correct and shall be *prima facie* evidence of a penalty due under this Section. Proof of such determination by the Department shall be made at any hearing before it or in any legal proceeding by reproduced copy of the Department's record relating thereto in the name of the Department under the certificate of the Director of Revenue. Such reproduced copy shall, without further proof, be admitted into evidence before the Department or any legal proceeding and shall be *prima facie* proof of the correctness of the penalty due, as shown thereon." Ill.Rev.Stat. 1991, ch. 120, par. 452½.

For guidance in determining the meaning of “willful” under section 13½, the Illinois Supreme Court has referred to cases interpreting section 6672 of the Internal Revenue Code (26 U.S.C. §6672)³. See Branson at 254-56; Department of Revenue v. Heartland Investments, Inc., 106 Ill.2d 19, 29-30 (1985). These cases define willful as involving intentional, knowing and voluntary acts or, alternatively, reckless disregard for obvious known risks. Id. Willful conduct does not require bad purpose or intent to defraud the government. Branson at 255; Heartland at 30. Willfulness may be established by showing that the responsible person (1) clearly ought to have known that (2) there was a grave risk that the taxes were not being paid and (3) the person was in a position to find out for certain very easily. Wright v. United States, 809 F.2d 425, 427 (7th Cir. 1987). Furthermore, whether the person in question willfully failed to pay the taxes is an issue of fact to be determined on the basis of the evidence in each particular case. Heartland at 30; Department of Revenue v. Joseph Bublick & Sons, Inc., 68 Ill.2d 568, 577 (1977).

The respondents argue that their actions were not willful because they believed that the corporation’s motor fuel tax obligations to the Department had been paid in full with the \$60,000 payment after the sale of the assets. They also claim that the corporation lacked adequate funds to pay the Department. They state that the penalty should not be imposed because during the last months of operation, the corporation’s major supplier would not deliver supplies without payment in advance, and the corporation owed more than \$50,000 to creditors after the sale of the assets.

The liability for the motor fuel taxes attached at the time that they were collected. See Anderson v. United States, 855 F.Supp. 236, 238 (N.D. Ill. 1994). The responsible officer had a duty to keep the taxes in trust from the day that the taxes were collected, regardless of the due date of the tax return. Id. The responsible officer was obligated to

³ This section imposes personal liability on corporate officers who willfully fail to collect, account for, or pay over employees' social security and Federal income withholding taxes.

use unencumbered funds to satisfy the tax obligations. Huizinga v. United States, 93-2 USTC ¶50470. Courts have found that if the responsible person knowingly uses available funds to pay other creditors, then he has acted willfully. Anderson at 238; Heartland at 29-30.

The evidence in this case supports a finding that the respondents' actions were willful. The respondents knew that the corporation was having financial difficulties and were aware of the corporation's tax obligations. JOHN DOE admitted that a return was not filed for July 1991. Although they claim that the corporation did not have adequate funds to pay the Department, several checks were issued to various unsecured creditors during the months in question. The payments to unsecured creditors were made without either respondent seeking assurance that the corporation's tax obligations were paid. With respect to the \$60,000 payment, the evidence does not indicate that either respondent sought verification that the payment fulfilled the corporation's tax obligations. The respondents have failed to show that their actions were not willful.

Recommendation

For the foregoing reasons, it is recommended that the Notices of Penalty Liability be upheld.

Linda Olivero
Administrative Law Judge

Enter: